F I S C A L   I M P A C T   R E P O R T

		ORIGINAL DATE	2/23/15		
SPONSOR	Herrell	**LAST UPDATED**	3/3/15	**HB**	520/aHWMC
SHORT TITLE	Military Acquisition Gross Receipts			**SB**	
				ANALYST	van Moorsel

REVENUE (dollars in thousands)

Estimated Revenue					**Recurring or Nonrecurring**	**Fund Affected**
FY15	**FY16**	**FY17**	**FY18**	**FY19**		
$0.0	$0.0	**Potentially Negative – See "Fiscal Implications"**			Recurring	General Fund
$0.0	$0.0	**Potentially Negative – See "Fiscal Implications"**			Recurring	Local Governments

Parenthesis ( ) indicate revenue decreases

Duplicates SB 448

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Department of Military Affairs (DMA)

SUMMARY

Synopsis of HWMC Amendment

The House Ways and Means Committee amendments restore a sunset date to the bill. As amended, the deduction would sunset at the end of FY25.

The amendments also impose a reporting requirement pursuant to which TRD must compile annual reports on the deduction and present the report to the Revenue Stabilization and Tax Policy committee and the LFC each year the deduction is in effect.

Synopsis of Original Bill

House Bill 520 amends the Gross Receipts and Compensating Tax Act to extend the deduction from gross receipts of receipts from transformational acquisition programs performing research and development, test and evaluation at New Mexico Major Range with the United States Department of Defense.

Under current law the deduction applies to gross receipts through June 30, 2016, and this bill removes that sunset to make qualifying receipts deductible into perpetuity.

There is no effective date of this bill. It is assumed that the new effective date is 90 days after this session ends.

FISCAL IMPLICATIONS

TRD's 2014 Tax Expenditure report notes the department has no available data to estimate the fiscal impact of the existing deduction. It is possible the deduction may never have been claimed. The department's analysis of the bill reports the fiscal impact of the deduction is indeterminate

However, TRD's FIR notes there may be new missions coming to Cannon Air Force Base and Holloman Air Force Base in the next few years that may bring taxpayers eligible for the deduction. Current law provides that the gross receipts of such activity are taxable beginning in FY17, and this bill would remove such gross receipts from the taxable base. As such, extension of the deduction would have a negative on the general fund and on local governments, assuming the contracts would have been entered into in the absence of the deduction. Because of the lack of information on this deduction, the size of any potential impact is indeterminate.

To illustrate, assuming a GRT rate of 7 percent, a $5 million contract for transformational acquisition programs would represent approximately $350 thousand in gross receipts tax, approximately $210 thousand of which is general fund revenue and $140 thousand of which is local government revenue.

This bill may be counter to the LFC tax policy principle of adequacy, efficiency and equity. Due to the increasing cost of tax expenditures revenues may be insufficient to cover growing recurring appropriations.

Estimating the cost of tax expenditures is difficult. Confidentiality requirements surrounding certain taxpayer information create uncertainty, and analysts must frequently interpret third-party data sources. The statutory criteria for a tax expenditure may be ambiguous, further complicating the initial cost estimate of the expenditure's fiscal impact. Once a tax expenditure has been approved, information constraints continue to create challenges in tracking the real costs (and benefits) of tax expenditures.

SIGNIFICANT ISSUES

The department may wish to promulgate rules to add clarity to the definition of "transformational acquisition programs" to facilitate data collection on the deduction.

TRD's 2014 Tax Expenditure report states the deduction is presumably to incentivize the location of military transformational acquisition programs at US Air Force bases in New Mexico. The deduction was originally enacted in 2005 with a sunset of June 30, 2008 before being amended in 2006 to extend the sunset to June 30, 2016.

The Department of Military Affairs' analysis reports:

> New Mexico is in a very competitive situation for economic development and military mission related projects. Though our State's bases have many technical advantages and the test facilities at the White Sands Missile Range and the Air Force Research Laboratory at Kirtland Air Force Base are world class, the test ranges are only resourced to 50%. The remaining required resources to operate and sustain the ranges are earned from "customers' paying to use the range capabilities (equipment, airspace, and personnel). This deduction allows the costs of using our bases to remain competitive with other competitor bases around the US.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is <u>not</u> met since TRD is <u>not</u> required in the bill to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose. ***The HWMC amendment added a reporting requirement to the bill.***

TECHNICAL ISSUES

This bill removes a sunset date. The LFC recommends a sunset date to require periodic review of the effectiveness of a tax expenditure. ***The HWMC amendment restored a sunset to the bill.***

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

PvM/je/aml